MULTIMEDIA UNIVERSITY

STUDENT ID NO

MULTIMEDIA UNIVERSITY

FINAL EXAMINATION

TRIMESTER 1, 2019/2020

BFN3084 – INTERNATIONAL FINANCE

(All sections / Groups)

25th October 2019
9.00 AM – 11.00 AM

(2 Hours)

INSTRUCTIONS TO STUDENTS

1. This Question paper consists of **3 pages** with **4 Questions** only.
2. Attempt **ALL** questions. All questions carry equal marks and the distribution of the marks for each question is given.
3. Please print all your answers in the Answer Booklet provided.

QUESTION 1 (25 MARKS)

ZoeInc and ZacCorp can borrow for a ten-year term at the following rates:

	ZoeInc	ZacCorp
Moody's credit rating	AA	BB
Fixed rate borrowing cost	8%	12%
Floating rate borrowing cost	LIBOR	LIBOR+3%

a. Calculate the quality spread differential (QSD). **(5 marks)**

b. Develop an interest rate swap in which both ZoeInc and ZacCorp have an equal cost savings in their borrowing costs. Assume ZoeInc desires floating-rate debt and ZacCorp desires fixed-rate debt. No swap bank is involved in this transaction.

(4 marks)

c. Do problem (b) over again, this time assuming more realistically that a swap bank is involved as an intermediary. The swap bank wants to earn 0.5% from the total cost saving and ZoeInc and ZacCorp will share the balance of cost saving equally. You are required to act as a swap bank to construct swap transactions for ZoeInc and ZacCorp. Please provide detailed transactions for each of the three counter parties with an illustration chart.

(16 marks)

QUESTION 2 (25 MARKS)

You plan to visit one of your friends living in Montana, America in three months. You expect to incur the total cost of US$15,000 for lodging, meals and transportation during your stay. As of today, the spot exchange rate is RM4.04/ US$ and the three-month forward rate is RM4.1/ US$. You can buy the three-month call option on US$ with the exercise rate of RM4.12/ US$ for the premium of RM1 per US$. Assume that your expected future spot exchange rate is the same as the forward rate. The three-month interest rate is 3.5 percent per annum in Malaysia and 2 percent per annum in the United States.

a. Calculate your expected ringgit cost of buying US$15,000 if you choose to hedge via call option on US$.

(7 marks)

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b. Calculate the future ringgit cost of meeting this US$ obligation if you decide to hedge using a forward contract. **(5 marks)**

c. At what future spot exchange rate will you be indifferent between the forward and option market hedges? **(5 marks)**

d. Illustrate the future ringgit costs of meeting the US$ payable against the future spot exchange rate under both the option and forward market hedges. **(8 marks)**

QUESTION 3 (25 MARKS)

Currently, the spot exchange rate is €0.9/$ and the three-month forward exchange rate is €0.95/$. The three-month interest rate is 3.0% per annum in the U.S. and 2% per annum in France. Assume that you can borrow as much as $1,000,000 or €900,000.

a. Determine whether the interest rate parity is currently holding. **(7 marks)**

b. If the IRP is not holding, how would you carry out covered interest arbitrage? Show all the steps and determine the arbitrage profit. **(12 marks)**

c. Explain how the IRP will be restored as a result of covered arbitrage activities. **(6 marks)**

QUESTION 4 (25 MARKS)

a. Describe the key factors contributing to effective cash management within a firm. Why is the cash management process more difficult in a MNC? **(10 marks)**

b. Recently, many foreign firms from both developed and developing countries acquired high-tech U.S. firms. What might have motivated these firms to acquire U.S. firms? **(8 marks)**

c. U.S. MNCs, such as Dell, HP, etc., made extensive investments in the Southeast Asian countries like Thailand, Malaysia and Indonesia. In your opinion, what forces are driving U.S. investments in the region? **(7 marks)**

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